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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)

Inquiry into Policies and)
Programs to Assure Universal)
Service in a Competitive)
Market Environment)

RM 8388

DEC 16 1993

COMMENTS OF
CATHEY, HUTTON & ASSOCIATES, INC.

FCC-MAIL

Cathey, Hutton & Associates, Inc. (CHA), management and cost consultants to the independent telephone industry, hereby comments on the "Petition of MFS Communications Company, Inc. for a Notice of Inquiry and *En Banc* Hearing" (MFS Petition) filed on November 1, 1993, in the above-captioned matter.

I. INTRODUCTION

MFS requests that the Commission initiate an investigation to "determine future policies for continuing to promote universal telephone service in a competitive market."¹ MFS sees this investigation as complimenting other proceedings such as those regarding access reform and related matters.²

CHA welcomes MFS's Petition and believes that an inquiry into universal service and future policies related thereto is long overdue. CHA is particularly encouraged by the recognition

¹ MFS Petition, p. ii.

² Id. at 8.

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that all providers of telecommunications services, including MFS, should "participate in the funding of universal service goals."³

CHA is concerned, however, with the general tenor of MFS's Petition which suggests that current universal service mechanisms result from dark motives of the local exchange carrier (LEC) industry. As discussed below, this is not the case at all, and any inquiry into universal service must be approached without the bias which permeates MFS's discussion.

MFS's Petition also demonstrates a total lack of understanding of how telecommunications services are delivered in rural areas. As explained below, this results in MFS making summary conclusions about support flows to high-cost areas that have no logical or factual foundation.

Finally, CHA opposes MFS's proposal that the National Exchange Carrier Association (NECA) should not administer universal service programs.⁴ Despite MFS's call for a "neutral party," NECA has already proven itself as a competent, fair and efficient administrator.

II. DISCUSSION

A. An Inquiry into Universal Service Policies and Programs Must Not Reflect the Bias Shown by MFS's Petition.

MFS's Petition is replete with innuendo and disparaging comments about the LEC industry, obviously intending to paint a

³ Id. at 9.

⁴ MFS Petition, pp. 17-18.

picture of some grand LEC plan to perpetuate subsidies as a way to limit local exchange competition. Thus, MFS refers to LECs as "entrenched monopolists" and accuses some LECs of propagating a "big myth" about the relation of subsidies to competition.⁵ MFS also claims that the LEC industry has made "grossly overstated"⁶ and "highly suspect"⁷ claims. Further, MFS attacks LEC bona fides by saying that LECs have "attempted to raise 'fear, uncertainty and doubt'"⁸ and by asserting that "LECs obviously have every incentive to inflate the apparent amount of subsidy to delay and frustrate the evolution of a competitive market."⁹

MFS, of course, is not the first party to use heated rhetoric in a Commission filing. Such spurious attacks, however, have no place in a proceeding which, if initiated, will largely determine whether the promised benefits of the Information Age will be made available to all Americans. Only objective analysis, and a careful weighing of sometimes conflicting goals, will ensure a reasoned decision on universal service policies appropriate for a rapidly changing telecommunications industry.

Additionally, while MFS recognizes that the goal of universal service is at the heart of the Communications Act of

⁵ MFS Petition, pp. ii, 2.

⁶ Id. at 11.

⁷ Id. at 19.

⁸ Id. at 2.

⁹ Id. at 14. See also p. 17 where MFS refers to the LECs' "clearly selfish economic incentives."

1934,¹⁰ MFS appears to lose sight of the fact that the present system of subsidies and high-cost support programs is the product of over 60 years of federal and state policies, and not the result of sinister motives on the part of the LEC industry. These policies were adopted during a period of little or no competition in the local exchange, and changing competitive conditions in the industry clearly warrant a review at this time. This does not mean, however, that there should be a wholesale abandonment of current support programs, or that the desire to promote competition should take preference over all other public interest objectives including the goal of ubiquitous deployment of advanced and affordable telecommunications services. It does mean that competition is an important consideration in fashioning national telecommunications policy and needs to be reflected in any future universal service programs that may be adopted.

In sum, CHA urges the Commission to issue a Notice of Inquiry on universal service policies. This inquiry must make an objective assessment of policy modifications necessary to achieve fundamental universal service objectives at a time of increasing competition and other major changes in the telecommunications industry. This inquiry must not be swayed by the kind of anti-LEC rhetoric contained in MFS's Petition.

¹⁰ MFS Petition, pp. 1-2, citing 47 U.S.C. § 151.

B. MFS Seriously Misconstrues How Telecommunications Services Are Delivered in Rural Areas.

Much of MFS's argument is targeted at support mechanisms that help to bring advanced and affordable telecommunications services to high-cost, rural areas. In particular, MFS objects to the distribution of funds to high-cost LECs "either directly through the USF or indirectly through the NECA Common Line Pool and such cost-shifting mechanisms as triple DEM weighting."¹¹ MFS questions whether a blanket subsidy to high-cost LECs is warranted, as opposed to "more targeted subsidies based on income, disability, and other customer characteristics that would assure the continued availability of basic service to all individuals."¹²

While targeted subsidies might be warranted under certain circumstances, MFS's proposal is undermined by its total lack of understanding concerning the delivery of telecommunications services in rural areas.¹³ Further, if by "targeted" MFS means eliminating direct support for LECs, as it appears,¹⁴ MFS's proposal should be rejected at the outset.

¹¹ MFS Petition, p. 10.

¹² Id. at 10-11.

¹³ This lack of understanding is not surprising since MFS has concentrated almost exclusively on serving customers in densely populated, generally lower-cost, urban areas.

¹⁴ See MFS Petition, p. 12; see id. at 6.

Among other misguided assertions, MFS states that "thanks in part to [high-cost support] programs, telephone service often costs less in rural areas and the territories of small LECs than it does in urban areas, leading to the extraordinary result that the service that costs more to provide is offered at a lower price."¹⁵ There is nothing extraordinary about this result at all. State public service commissions often require rural local exchange service to be priced lower than urban local exchange service because the rural telephone subscriber can reach only a small fraction of the number of telephones available in an urban exchange area. Even with extended area calling, rural residents often must make toll calls to reach schools, churches, doctors, businesses and other parties within their community of interest that urban callers take for granted as local calls. Thus, while the price of exchange service is sometimes lower in rural areas, the total cost of using the public switched network is often far higher in rural areas than in urban areas. The calling scope of the rural exchange subscriber and the high total charges for rural telephone service must be considered in any proceeding looking at universal service policies.

MFS also suggests "that rural areas should, as a general proposition, be expected to pay their own way for telephone service just as urban areas pay their own way for housing."¹⁶ MFS is apparently unaware of federal and state programs which

¹⁵ Id. at 10.

¹⁶ Id. at 11.

offer low-cost housing subsidized by taxes paid by both urban and rural residents, or of the indirect subsidies made to individuals, regardless of ability to pay, through the tax system's mortgage interest deduction.¹⁷

MFS further contends that "subsidy programs should initially be limited to POTS access, including Touch-Tone (or DTMF) signalling."¹⁸ Although MFS continues by stating that the "universal service goal should be designed to allow all Americans to be *connected* to the ubiquitous public switched network . . . ,"¹⁹ MFS fails to consider that advanced capabilities are required in the public switched network so that rural areas do not become the Route 66 of the Information Age.

Moreover, MFS's position that support programs be limited to providing a "plain vanilla" public switched network is inconsistent with the intent of Congress as expressed in the recently enacted Rural Electrification Loan Restructuring Act of

¹⁷ The economics of the delivery of housing and telephone service are also quite different and, thus, require different subsidy approaches. For example, housing is constructed in discrete, individualized units where the purchaser can be charged a price that covers all the costs associated with the purchased unit. In contrast, because local telephone service is not produced in discrete units, but requires a common network, there are substantial common costs which are not easily recoverable when subscriber densities are low, as is often true in rural areas. Thus, even when average subscriber incomes are high, as in the few locations cited by MFS (Petition, p. 11), reasonable local rates will often not recover all costs incurred in providing an advanced telecommunications infrastructure. The existence of substantial common costs also makes it more difficult to target subsidies at individuals.

¹⁸ MFS Petition, p. 10.

¹⁹ Id. (emphasis in original).

1993. That Act requires each state, in order for LECs to qualify for Rural Electrification Administration (REA) loan programs, to develop a telecommunications modernization plan that must include, inter alia, (1) the availability of tele-communications services for improved business, educational and medical services; (2) the availability to rural subscribers of conference calling, video images and data at a rate of at least 1 million bits of information per second; and (3) uniform deployment schedules to assure that advanced services are deployed at the same time in rural areas and non-rural areas. Any proceeding on universal service must consider these factors as minimum requirements for developing the public switched network infrastructure in rural areas.

Finally, MFS states that high-cost support "programs are plainly incompatible with increasingly competitive markets."²⁰ MFS states further that "it is hard to imagine why any competitor would want to serve a rural area if the incumbent LEC is subsidized and the new entrant has to compete based on its own costs."²¹

MFS argument might make sense were it not for the fact that the incumbent LEC has "carrier of last resort" responsibility to serve all rural subscribers regardless of costs. Under such circumstances, it would be foolhardy to eliminate high-cost support on the chance that someday a

²⁰ Id. at 12.

²¹ Id.

competitor might decide to serve part of a rural market. Until a competitive service provider will assume responsibility for all subscribers in a particular area, high-cost support paid directly to the LEC is essential if all such subscribers are to obtain affordable and advanced telecommunications services.

C. NECA Should Continue as the USF Administrator.

MFS proposes that the "Commission provide for designation of a disinterested third-party administrator for all subsidy programs."²² MFS believes that this is necessary because of an alleged potential for bias on the part of NECA, the current administrator of USF and other support mechanisms.²³

CHA notes that while the potential for a conflict of interest could arise with regard to some of NECA's activities,²⁴ no one has ever questioned the integrity of NECA's processes or has ever alleged any irregularities or improprieties in the way NECA administers the current universal service programs. Indeed, NECA's role in the Commission's support programs is just that - administrative. NECA has very little discretion that can be influenced by what MFS incorrectly perceives as pro-LEC bias.

In short, NECA has proven that it can administer universal service programs in an efficient and even-handed manner. So long

²² MFS Petition, p. 17.

²³ Id.

²⁴ An extended discussion on the proper scope of NECA's activities is set forth in CHA's Comments, filed November 22, 1993, in AAD 93-126, concerning NECA's request for authorization to perform additional services.


as NECA's activities are in furtherance of the purposes for which it was created - and the administration of support mechanisms for the LEC industry certainly is within those purposes - there is no reason for the Commission to terminate NECA's involvement with universal service programs.

III. CONCLUSION

CHA supports MFS's call for an inquiry on universal service policies. Such an inquiry, however, must be fashioned and conducted in an objective and even-handed manner, without the obvious bias that permeates MFS's Petition. Additionally, the inquiry cannot cavalierly dismiss, as does MFS, the special needs and circumstances of rural telephone service providers and subscribers. Finally, NECA remains the most competent and appropriate party to administer support programs.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Marcella C. Jost, do hereby certify that copies of the foregoing Comments of Cathey, Hutton & Associates, Inc. were sent via first class mail, postage paid, to the following on this the 16th day of December, 1993:

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